



# Joint Legislative Audit Committee

OFFICE OF THE AUDITOR GENERAL

## California Legislature



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LOS ANGELES

February 13, 1978

Letter Report 282.5

The Honorable Speaker of the Assembly  
The Honorable President pro Tempore of the Senate  
The Honorable Members of the Senate and the  
Assembly of the Legislature of California

Members of the Legislature:

I am pleased to forward the Auditor General's letter report supplementing his Report No. 282.4 relating to deficiencies in product cost determinations of the Correctional Industries Program in fiscal year 1976-77. The latter report raised the question as to whether it was proper to utilize profits of the manufacture of license plates and validation stickers to support the overall operations of the program. This letter report contains an opinion of the Legislative Counsel that it is improper and is prohibited by the California Constitution.

The auditors are Harold L. Turner, Audit Manager; Robert J. Maloney; and Walter M. Reno.

Cordially,

MIKE CULLEN  
Chairman



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February 9, 1978

Letter Report No. 282.5

Honorable Mike Cullen  
Chairman, and Members of the  
Joint Legislative Audit Committee  
Room 5144, State Capitol  
Sacramento, California 95814

Dear Mr. Chairman:

Our report number 282.4 issued on December 15, 1977, entitled Deficiencies in Correctional Industry Product Cost Determinations, identified the financial status of the Correctional Industries program by specific industry. The report indicated that for fiscal year 1976-77, ten industries operated at a combined profit of \$1,200,000 and eighteen industries operated at a combined loss of \$1,559,000, resulting in an overall net loss of \$359,000 in the Correctional Industries Revolving Fund.

Of the \$1.2 million profits, we determined that \$863,000 was contributed by two industries: the license plate factory at Folsom State Prison, \$517,000, and the Specialty Printing industry at the California Men's Colony, \$346,000, which produces motor vehicle license plate validation stickers. The profits of these two industries are used to offset the losses of other industries in the Correctional Industries Revolving Fund.

The monies used by the Department of Motor Vehicles to purchase license plates and motor vehicle validation stickers come from the Motor Vehicle Account and are earmarked for transportation purposes under Article XIX of the California Constitution. Subsequent to our report, we asked the Legislative Counsel for an opinion on the appropriateness of using the profits earned from the sale of license plates and validation stickers to offset other industries' losses (Appendix A). The opinion from the Legislative Counsel (Appendix B) stated that if monies paid by the

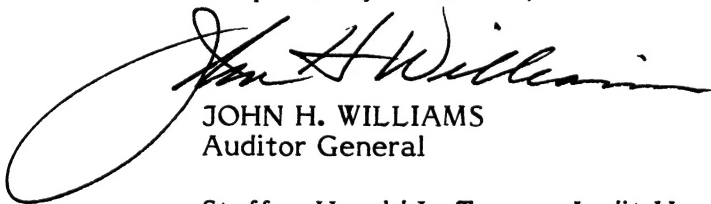
Honorable Mike Cullen  
Chairman, and Members of the  
Joint Legislative Audit Committee  
February 9, 1978  
Page 2

Department of Motor Vehicles are in excess of the costs incurred by Correctional Industries to produce license plates and validation stickers, and if these profits come from transportation-related funds, they can only be used for transportation purposes as specified by Article XIX of the California Constitution. Consequently, in the Legislative Counsel's opinion, the \$863,000 in profits that we determined were earned from the sale of license plates and stickers cannot be used to offset the costs of producing other industry products within the Correctional Industries program and such use would be unconstitutional.

Recommendation

To insure that monies from the Motor Vehicle Account Fund are used in compliance with Article XIX of the California Constitution, Correctional Industries should develop an accounting system that identifies the actual costs of producing license plates and validation stickers, including an appropriate share of overhead costs, in order to charge the Department of Motor Vehicles only those costs that are appropriate. In addition, to insure that appropriate charges are being made by Correctional Industries, the Department of Finance or the Department of Motor Vehicles should conduct periodic audits of the license plates and motor vehicle validation sticker charges made to the Department of Motor Vehicles.

Respectfully submitted,



JOHN H. WILLIAMS  
Auditor General

Staff: Harold L. Turner, Audit Manager  
Robert J. Maloney  
Walter M. Reno

Attachments: Written Responses to the Auditor General's Report

Director, Department of Corrections

Director, Department of Motor Vehicles

Appendix A--Request for Legislative Counsel Opinion  
dated December 6, 1977

Appendix B--Legislative Counsel Opinion  
dated December 29, 1977

## DEPARTMENT OF CORRECTIONS

SACRAMENTO



February 8, 1978

Mr. John H. Williams  
Auditor General  
California Legislature  
925 L Street, Suite 750  
Sacramento, California 95814

Dear Mr. Williams:

This responds to your January 27 letter concerning the draft of your report on Correctional Industries.

I appreciate the opportunity to comment. I must respectfully disagree with one of the report's basic contentions.

It is my position that profits to the Correctional Industries Revolving Fund from the manufacture of license plates and validation stickers are quite properly used to support the overall operation of Correctional Industries--in the same way that revenue from any source is used to cover costs and losses.

The charge by Correctional Industries for the manufacture of license plates and validation stickers is fair and consistent with law which requires pricing "as near prevailing market price as possible."

Once DMV has made payment, it is in my view completely appropriate for the recipient, whether Industries or some other manufacturer or vendor, to use such monies in its operation.

I would be pleased to discuss this at some mutually convenient time. Again, thanks for the opportunity to comment.

Sincerely,

A handwritten signature in dark ink, appearing to read "J. J. Enomoto", written over a horizontal line.

J. J. ENOMOTO  
Director of Corrections  
445-7688

cc: Mr. E. Becky

OFFICE OF THE DIRECTOR

**DEPARTMENT OF MOTOR VEHICLES**

P. O. BOX 1828  
SACRAMENTO, CA 95809

(916) 445-3866



February 7, 1978

Mr. John H. Williams  
Auditor General  
Legislative Audit Committee  
925 L St., Suite 750  
Sacramento, CA 95814

Dear Mr. Williams:

We have reviewed with concerned interest the Report to the California Legislature, "Deficiencies in Correctional Industry Product Cost Determinations", (Report Number 282.4) dated December 19, 1977, together with the accompanying Letter Report No. 282.5, dated January 1978, to the Honorable Mike Cullen, Chairman, and Members of the Joint Legislative Audit Committee.

The sections of the above-referenced reports that impact the Department of Motor Vehicles relate to the opinion of the Legislative Counsel that the use of Motor Vehicle Account Funds to secure license plates and stickers from the Department of Corrections for a charge in excess of actual cost is in violation of Article XIX of the California Constitution.

This opinion creates an apparent conflict with the requirements of Section 2871 of the California Penal Code, which mandates that: "The Director (of Corrections) shall determine the price at which articles, materials and supplies shall be sold, which price shall be as near the prevailing market price as possible."

We have not had an opportunity to validate or analyze the cost figures for license plates and stickers reflected in the report due to time constraints in responding to your request.

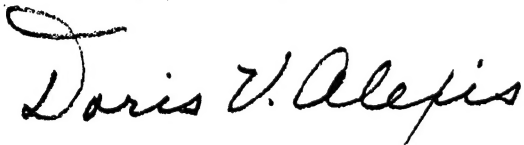
You have specifically recommended that to insure appropriate charges are being made by Correctional Industries, the Department of Finance or the

Department of Motor Vehicles should conduct periodic audits of the license plates and motor vehicle validation sticker charges made by the Department of Corrections.

The Department of Motor Vehicles concurs in the recommendation with the following exceptions:

1. The apparent conflict between the Legislative Counsel's opinion in reference to Article XIX California Constitution and Section 2871 California Penal Code should be resolved; and,
2. Periodic audits should be conducted by the Department of Finance as that Agency is charged with this responsibility under the Government Code. The Department of Motor Vehicles will assist in the audits as determined appropriate by the Department of Finance.

Sincerely,

A handwritten signature in cursive script that reads "Doris V. Alexis". The signature is written in dark ink and is positioned above the typed name and title.

DORIS V. ALEXIS  
Director



# Joint Legislative Audit Committee

APPENDIX A

OFFICE OF THE AUDITOR GENERAL

## California Legislature



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### M E M O R A N D U M

DATE: December 6, 1977

TO: Legislative Counsel

FROM: Peter A. Barbosa

SUBJECT: Legal Opinions

#### Background

Correctional Industries manufactures license plates and stickers which the Department of Motor Vehicles is required to purchase from Correctional Industries. The funds for these purchases are provided by the Motor Vehicle Fund. The price charged the Department of Motor Vehicles results in \$863,000 profit to Correctional Industries after deducting all direct costs and assigning a fair proportion of administrative overhead.

Given that both Department of Motor Vehicles and Correctional Industries are state agencies and that the \$863,000 profit is used by Correctional Industries to subsidize or support the manufacture of other nontransportation products (i.e., furnishings, milk, clothing) used by nontransportation agencies (i.e., school districts, counties, other state agencies).

#### Questions

1. Is use of the Motor Vehicle Fund monies permitted by the State Constitution to support the Correctional Industries program?
2. Is the profit paid to Correctional Industries by the Department of Motor Vehicles allowable under present statutes?
  - a. If not--does the Department of Motor Vehicles have the authority to recover those profits from Correctional Industries?
  - b. If so--does the fact that the profit to Correctional Industries represents 72 percent of the total profits earned by Correctional Industries create any concerns as to "fair and reasonable?"

OWEN K. KUNS  
RAY H. WHITAKER  
CHIEF DEPUTIES

STANLEY M. LOURIMORE  
EDWARD F. NOWAK  
EDWARD K. PURCELL

KENT L. DECHAMBEAU  
HARVEY J. FOSTER  
ERNEST H. KUNZI  
SHERWIN C. MACKENZIE, JR.  
ANN M. MACKEY  
TRACY O. POWELL, II  
RUSSELL L. SPARLING  
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8011 STATE BUILDING  
107 SOUTH BROADWAY  
LOS ANGELES 90012  
(213) 620-2550

APPENDIX B

# Legislative Counsel of California

BION M. GREGORY

Sacramento, California  
December 29, 1977

GERALD ROSS ADAMS  
DAVID D. ALVES  
MARTIN L. ANDERSON  
PAUL ANTILLA  
JEFFREY D. ARTHUR  
CHARLES C. ASBILL  
JAMES L. ASHFORD  
JERRY L. BASSETT  
JOHN CORZINE  
BEN E. DALE  
CLINTON J. DEWITT  
C. DAVID DICKERSON  
FRANCES S. DORBIN  
ROBERT CULLEN DUFFY  
CARL ELDER  
LAWRENCE H. FEIN  
JOHN FOSSETTE  
CLAY FULLER  
ALVIN D. GRESS  
ROBERT D. GRONKE  
JAMES W. HEINZER  
THOMAS R. HEUER  
EILEEN K. JENKINS  
MICHAEL J. KERSTEN  
L. DOUGLAS KINNEY  
VICTOR KOZIELSKI  
JAMES A. MARSALA  
DAVID R. MEEKER  
PETER F. MELNICOE  
ROBERT G. MILLER  
JOHN A. MOGER  
VERNE L. OLIVER  
EUGENE L. PAINE  
MARGUERITE ROTH  
MARY SHAW  
WILLIAM K. STARK  
JOHN T. STUDEBAKER  
DANIEL A. WEITZMAN  
THOMAS D. WHELAN  
JIMMIE WING  
CHRISTOPHER ZIRKLE  
DEPUTIES

Honorable Mike Cullen  
5144 State Capitol

Expenditures for License Plates - #17150

Dear Mr. Cullen:

QUESTION

You have asked us to assume the following:

That appropriations to the Department of Motor Vehicles<sup>1</sup> from the Motor Vehicle Account in the State Transportation Fund<sup>2</sup> for the purchase of license plates manufactured under the jurisdiction of the Correctional Industries Commission<sup>3</sup> does not reflect the actual cost of the plates and that a large percentage of the appropriations is used by Correctional Industries to reimburse Correctional Industries for costs incurred by them in the production of goods and products sold to other state agencies not related to authorized transportation purposes (e.g. office furnishings, milk, clothing) as specified in Article XIX of the California Constitution.<sup>4</sup>

- 
- 1 Hereinafter referred to as the department.
  - 2 Hereinafter referred to as the Motor Vehicle Account.
  - 3 Hereinafter referred to as Correctional Industries.
  - 4 Hereinafter referred to as Article XIX.



Based on the above assumption, you have asked whether such use of funds from the Motor Vehicle Account is in violation of the provisions of Article XIX.

#### OPINION

Based on the above assumption, such use of funds from the Motor Vehicle Account is in violation of the provisions of Article XIX.

#### ANALYSIS

Under Article XIX, highway revenues (i.e., revenues from the state-imposed gas tax, diesel fuel tax, registration fees, weight fees, and driver's license fees)<sup>5</sup> may be used for the research, planning, construction, improvement, maintenance, and operation of public streets and highways (including related public facilities for nonmotorized traffic) and for the acquisition of property and administrative costs therefor, and for the mitigation of public street and highway environmental effects (subd. (a), Sec. 1, Art. XIX, Cal. Const.; Secs. 7351, 8351, 8353, 8651, 9301, 9303, R. & T.C.; Sec. 2101, S. & H.C.; Secs. 9250 et seq., 9400 et seq., 14900 et seq., 42270, 42271, 42273, Veh. C.).

The highway revenues may also be used for similar purposes for exclusive public mass transit guideways, and related fixed facilities, except for the maintenance and operation of mass transit power systems and mass transit passenger facilities, vehicles, equipment, and services (subd. (b), Sec. 1, Art. XIX, Cal. Const.; Secs. 200, 2101, S. & H.C.). However, before the highway revenues may be used for such guideway purposes, except for research and planning on such guideways, in any area, a proposition authorizing such use of the highway revenues must be approved by a majority of the votes cast on the proposition in the area (Sec. 4, Art. XIX, Cal. Const.; Secs. 199, 2101, S. & H.C.).

With respect to highway revenues derived from vehicles (i.e., registration fees, weight fees, and driver's license fees), these revenues may also be used for the enforcement of traffic and vehicle laws by the state and for the mitigation of the environmental effects of motor vehicle operation due to air and sound emissions (Sec. 2, Art. XIX, Cal. Const.; Sec. 42271, Veh. C.).

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<sup>5</sup>

The revenues derived from taxes imposed pursuant to the Sales and Use Tax Law or the Vehicle License Fee Law are exempt from Article XIX (Sec. 7, Art. XIX, Cal. Const.).

Pursuant to Section 42270 of the Vehicle Code, the department collects, for eventual deposit into the Motor Vehicle Account in the Transportation Tax Fund, various registration, weight, drivers license, service and related fees.

Moneys from the Motor Vehicle Account are used to, among other things, support most operations of the department, including carrying out provisions of the Vehicle Code and enforcing other laws relating to vehicles or the use of the highways (subd. (b), Sec. 42271, Veh. C.).

Since revenues derived from motor vehicle fees and taxes are earmarked for special purposes, as discussed above, only programs effectuating these purposes may be funded from this source. Thus, unless a program involves the administration and enforcement of laws regulating the use, operation, or registration of vehicles used upon public streets and highways, mitigation of the environmental effects of motor vehicle air and sound emissions, or research, planning, construction, improvement, maintenance, and operation of public streets, highways, or mass transit guideways and facilities, financing through the Motor Vehicle Account is not appropriate.

Obviously, the purchasing of license plates by the department for later issuance for display on vehicles is within the purview of Article XIX.

However, if the money paid to Correctional Industries for license plates does not reflect the actual cost of the plates and a large percentage of the money paid them by the department is used by Correctional Industries for reimbursement of costs incurred by them in the production of goods and products sold to other state agencies not related to transportation purposes, such use would not be proper under Article XIX.

Therefore, it is our opinion, based on the above assumption, that such use of funds from the Motor Vehicle Account is in violation of Article XIX.

Very truly yours,

Bion M. Gregory  
Legislative Counsel

By 

David D. Alves  
Deputy Legislative Counsel